## INDEX


| | Page |
|---|---|
| STATEMENT OF CASE | 1, 6 |
| ARGUMENT AND AUTHORITIES | 6, 18 |
| ANSWER TO POINT I | 7, 9 |
| ANSWER TO POINT II | 9, 10 |
| ANSWER TO POINT III | 10, 13 |
| ANSWER TO POINT IV | 13, 16 |
| ANSWER TO POINT V | 16, 17 |
| CONCLUSION | 17, 18 |


### STATUTES CITED


| | |
|---|---|
| Bankruptcy Act, Sec. 25, as amended, 52 Stat. 840, 855, 11 U.S.C.A., para. 48 | 7 |
| Rules of Civil Procedure of the District Courts of the State of New Mexico, 19-201 (5) of New Mexico Statutes Annotated, 1941 | 14 |


### CASES CITED


| | |
|---|---|
| Burns v. Fleming, 48 N. M. 40, 145 P. (2d) 861 | 15 |
| Foster v. Addington, 48 N. M. 212, 148 P. (2d) 373 | 15 |
| Gross v. Irving Trust Co., 286 U. S. 342 | 16, 17 |
| In Re. Prudence, 96 F. (2d) 157 | 12 |
| In Re: San Juan Gold, Inc., 96 F. (2d) 60 | 12, 13 |
| Nehr v. Crawford, 10 N. M. 725, 65 P. 156 | 13 |
| O'Hara v. Oakland Co., 136 F. (2d) 152 | 9 |
| Prichard v. Fulmer, 22 N. M. 134, 159 P. 39, 2 A.L.R. 474 | 7, 9 |
| Sherman v. Buckley, 119 F. (2d) 280 | 10, 11, 12, 17 |
| Taylor v. Sternberg, 293 U. S. 470 | 16 |

No. 641

IN THE

# Supreme Court of the United States

October Term, 1949

G. PULLEN JACKSON AND FRANK L. HORAN, a Partnership, practicing under the name of JACKSON AND HORAN, Petitioners,

v.

HARRY V. VANCE, Trustee of the Estate of WILLIAM O. STUART; and ALBUQUERQUE NATIONAL TRUST AND SAVINGS BANK, Respondents.

## BRIEF OF RESPONDENTS

### STATEMENT OF CASE

Deeming it necessary, the respondents, pursuant to paragraph 3 of Rule 27, of this Court, respectfully restate the case for the following reason:

In appealing the case to the Court of Appeals of the Tenth Circuit, the petitioners filed a skeleton transcript so brief as that the Court could not have determined the exact nature of the controversy (Tr. 1-18).

The respondents here, appellees there, filed a supplemental transcript in the Court of Appeals (Tr. 19-49). They feel that a chronological statement of facts now involved will assist the Court, and eliminate searching the transcript and the supplemental transcript, in an effort to rearrange the facts in chronological order.

Commencing July 30, 1946, and up to and including September 13, 1946, W. O. Stuart borrowed from the Albu-

querque National Trust and Savings Bank, upon five notes aggregating $58,850.00 (Tr. 35-41). He secured the Bank by depositing Douglas-Guardian Warehouse receipts on chattel property, written directly to the Bank (Tr. 41-42). He bought insurance on these goods, in his name, with a loss payable clause to the Bank, as its interest appeared, with three insurance companies, to-wit: Pacific National Fire Insurance Company, for $65,000.00, and American Home Fire Assurance Company, for $65,000.00, and the American Home Fire Assurance Company assigned half of its coverage to the New York Underwiters Insurance Company (Tr. 22).

Stuart owned other goods besides those covered by the Bank's warehouse receipts.

January 28, 1947, the goods were destroyed by fire.

February 1, 1947, Stuart employed Jackson and Horan, attorneys, to represent him in collecting the insurance upon a fee arrangement of 15%, without suit; 20%, if suit should be brought; and from 25% to 33 1/3%, if trial or appellate work was necessary (Tr. 1-2).

It is not claimed that the Bank had any part in employing these attorneys. On June 16, 1947, involuntary bankruptcy proceedings were filed against Stuart in the District Court of the United States for the District of New Mexico, and on the same day Jackson and Horan, as attorneys for Stuart, filed in the State Court a suit against the three insurance companies to recover the amount of the damage alleged to have been caused by the fire, aggregating $125,000.00 (Tr. 25).

The Bank, although holding warehouse receipts in its name, on what it alleges to be at least $60,000.00 in value

of the goods, was not made party defendant in the State Court, and there the matter rested.

July 14, 1947, respondent, Harry V. Vance, was elected trustee of the bankrupt estate of Stuart (Tr. 27).

August 14, 1947, Vance, as trustee, filed a motion in the State Court case, asking to be substituted as party plaintiff, which motion was filed by Threet and Hall, attorneys for the trustee (Tr. 25-26).

Jackson and Horan, as attorneys for Stuart, the plaintiff in the State Court case, attempted to resist the motion of the trustee to be substituted by other counsel, and moved to strike the trustee's motion. The State Court heard both motions together, and on the 21st of August 1947, denied Jackson and Horan's motion to strike the trustee's motion, granted the motion of the trustee to be substituted, and in the same order adjudged that Jackson and Horan had a charging and retaining lien as attorneys for Stuart, to secure a fee of 15% of the amount recovered in the cause, and the trustee excepted (Tr. 23).

On September 9, 1947, the trustee filed a second amended complaint in the State Court by his lawyers, Threet and Hall, setting up that he, as trustee for the estate of the bankrupt, owned the cause of action against the insurance companies, asking for judgment thereon, bringing in the Albuquerque National Trust and Savings Bank as a party defendant, and asking that the Bank be required to set up the extent and amount of its claims against the insurance fund (Tr. 26-33).

On the 9th of September 1947, the Bank filed its answer and cross-complaint (Tr. 35-47).

A year later on September 3, 1948, Jackson and Horan, who were not parties to the second amended complaint filed by the trustee in the State Court, nor to the cross-complaint of the Bank, without notice or bond, obtained an order to show cause and temporary restraining order from the State Court, prohibiting the defendant insurance companies from settling, compromising or entering into a stipulated judgment and settlement of the causes of action set forth in the second amended complaint, in neglect or disregard of the order of the State Court establishing the charging and retaining lien in favor of Jackson and Horan, and directing them to show cause (Tr. 47-48).

The statement made by the petitioners here in their Statement of the Case, on page 4 of their brief, as follows:

> "On September 3, 1948, petitioners discovered that the insurance companies, acting through their attorney, had entered into an agreement with the Albuquerque National Trust and Savings Bank for a stipulated judgment of $60,000.00 to be paid to the bank directly, ignoring petitioners' lien and bankruptcy proceeding."

is without support in the record, and we will not undertake to go outside the record to answer it. The improbability of a settlement in a large amount, by three insurance companies then under suit by the trustee, in disregard of the bankruptcy proceeding, would seem to be evident.

Faced with this State Court restraining order, the trustee appealed to Judge Neblett of the United States District Court in charge of the bankruptcy proceedings, and on October 25, 1948, the Federal Judge entered an order reciting that a compromise and settlement agreeable to all parties had been effected with the insurance com-

panies, and restraining Jackson and Horan from pursuing their claimed remedies in the State Court; directing them to dismiss their application for the restraining order; requiring the money under the settlement to be paid to the trustee in bankruptcy for administration in the bankruptcy Court, and holding that any rights of Jackson and Horan, which they might have as lien claimants should not be prejudiced, but that they should go into the bankruptcy proceeding with all their rights fully preserved; approving the action of a creditors' meeting accepting the compromise of $60,000.00 from the insurance companies, of which $35,000.00 was allocated to the security of the Bank, and $25,000.00 to the general funds of the estate, and directing both Jackson and Horan and the Bank to present their claims to the referee (Tr. 3-5). In obedience to this order the State Court case was dismissed with prejudice December 7, 1948 (Tr. 5).

The matter was heard by the referee; Jackson and Horan presented their claim for $9,000.00, being 15% of the compromise of $60,000.00, together with an unsecured claim of $2,836.81 (Tr. 7-8). The referee held that the order of the State Court, adjudging the charging and retaining lien in favor of Jackson and Horan, was res adjudicata of their right to collect their attorney's fees out of the proceeds of the settlement, but also held that it could only apply to the general funds of the estate in the amount of $25,000.00 and not to the Bank's secured portion, and gave judgment for Jackson and Horan for $3,750.00 (Tr. 9).

The matter was immediately reviewed by the trustee and the Bank, before District Judge Neblett, who, on February 15, 1949, entered an order adjudging that after the adjudication in bankruptcy of Stuart, June 19, 1947, three days

after he had filed his first complaint in the State Court against the insurance companies, the State Court was without jurisdiction to impress a charging and retaining lien in favor of Jackson and Horan upon the proceeds of such recovery as might be made upon the policies of insurance, and that the State Court's order was a nullity. He also held that Jackson and Horan had a right to file their claim before the referee and make proof of the value of their services, and that their payment could only come out of the $25,000.00 in the general funds, and no part thereof could be charged against the Bank (Tr. 10-12).

February 21, 1949, Jackson and Horan appealed to the Court of Appeals of the Tenth Circuit from both the order of October 25, 1948, and the order of February 15, 1949.

Speaking through Judge Bratton, the Court of Appeals affirmed the District Court, Judge Phillips concurring and Judge Murrah dissenting (Tr. 57). This petition for certiorari followed.

## ARGUMENT AND AUTHORITIES

At the outset, we may eliminate any question of the order of the U. S. District Court of October 25, 1948. That order restrained Jackson and Horan from further proceeding in the State Court and directed them to dismiss their application for a restraining order, and after requiring the fund to be derived from the settlement with the insurance companies to be paid over to the trustee for administration by the bankruptcy court, it is specifically adjudged that any rights of Jackson and Horan, which they now have as a lien claimant in the District Court, should not be prejudiced in any manner, but that they were made parties to the bankruptcy proceeding (in which they were also unse-

cured creditors), and their rights as lien claimants were fully preserved for consideration by the bankruptcy court, and the compromise settlement approved by the common creditors and the distribution thereof, as agreed on before the referee by all parties, was affirmed (Tr. 3-5).

In the opinion of the Court of Appeals, Judge Bratton pointed out that since no appeal was taken from this order of the District Court, within thirty days, under Section 25 of the Bankruptcy Act, as amended, *52 Stat. 840, 855, 11 U.S.C.A. paragraph 48,* the correctness of that order was not before the Court. Petitioners do not challenge this holding. Such being the condition of the record the petitioners are confined to a consideration of the order of the Federal District Court made on February 15, 1949 (Tr. 10-12), and affirmed by the Court of Appeals.

## POINT I

Under this Point, the petitioners say that the Trial Court erred in holding and finding that no lien had been created by the contract between Stuart and the petitioners, as confirmed by the order, judgment and decree of the State Court.

When Jackson and Horan, in obedience to the Federal Court order of October 25, 1948, presented their claim to the referee in bankruptcy, in the form of a motion to require the trustee to pay their claim of $9,000.00, they claimed a lien confirmed by court order, final in nature, a copy being attached and set forth, and stated that under the State Court order they had a prior lien over and above all other claimants on the fund of $60,000.00 (Tr. 6).

First, petitioners say that *Prichard v. Fulmer, 22 N. M. 134, 159 P. 39, 2 A.L.R. 474,* sustains their position. We

think not. New Mexico has no statute giving a charging or retaining lien to attorneys. The only question in the Prichard case was whether or not a lawyer who had foreclosed a mortgage for his cilents had a lien upon the real estate which they bought at the foreclosure sale. The Supreme Court answered in the negative. In the course of the opinion, the Court discussed the common law of charging and retaining liens, but went no further than to observe that the papers, documents and money of the client, which the lawyer had in his possession, were subject to such a lien. As applied to the facts of our present case, up to the time that the State Court on the 21st of August 1947, attempted to adjudicate and fasten a charging and retaining lien upon the ultimate proceeds of the suit against the three insurance companies, if, as and when liquidated and received, so far as the record here shows, Jackson and Horan had neither papers, documents or money belonging to their client, which they might claim to withhold from the trustee as successor in interest. There was no receivership. There was no property in possession of the State Court. It had before it only a suit for unliquidated damages on fire insurance policies, and an indispensable party, the Bank, had not been brought in, nor had the insurance companies filed any answer whatsoever. The State Court order of August 21, 1947, had nothing whatever upon which it could operate.

We do not have the question of the power of a State Court which has rendered a final judgment, and the process from which has effected collection, to prevent a client from defrauding his attorney out of the fee.

Petitioner's position here is tantamount to saying that a State Court can volunteer advice and binding instructions to the Federal bankruptcy court as to how the latter

shall treat lien claimants with reference to a fund of money if acquired in the future, by suit or compromise out of court.

The suggestion that the trustee, under the orders of the bankruptcy court, might so administer the recovery from the insurance companies as to defraud Jackson and Horan out of their just fee, would not seem to require extended discussion.

## POINT II

Under this Point, the petitioners say that United States District Court was in error when it enjoined Jackson and Horan from pursuing their restraining order in the State Court, directed against the insurance companies, because the State Court had jurisdiction to enforce its order, fixing the lien, and the United States Court was without jurisdiction in bankruptcy to interfere with the State Court's proceedings.

Here we have a startling statement. Petitioners claim that the Federal Court in charge of the bankruptcy proceedings must sit with its hands tied and allow a State Court to reach into the administration before the referee and direct the payment of attorneys as lien claimants, as a matter of legal right and authority. They again cite *Prichard v. Fulmer,* supra, which, as above stated, holds nothing of the kind. The fallacy in the petitioners' argument here, when they cite *O'Hara v. Oakland Co., 136 F. (2d), 152, 6 CCA,* is that neither the Prichard case nor the O'Hara case presented any question of conflict of jurisdiction between the State Court and the Federal bankruptcy court. In the O'Hara case there was no question of bankruptcy intervening, nor of the paramount jurisdiction of

the federal tribunal under the bankruptcy act. Likewise, in the Prichard case the decision which is dictum beyond the point where the Court held the lawyer had no lien on his client's land, there was no question or bankruptcy or which Court should yield to the other, as we now have here.

We will notice the other cases cited by the petitioners under Point II, under our argument in the next paragraph under Point III.

## POINT III

Under this Point, petitioners claim error in the action of the Federal District Court in holding that the State Court was without jurisdiction to award Jackson and Horan a lien on the fund which was created largely through their efforts.

At the outset, the Court will notice that Jackson and Horan created no fund; they merely filed an inadequate complaint in the State Court against three insurance companies, on the same day the involuntary petition in bankruptcy was filed against Stuart, to-wit, June 16, 1947. Whether Jackson and Horan succeeded in getting to the State Court a few minutes before or after the bankruptcy petition reached the Federal Court, the record does not show. The trustee could have dismissed this litigation and could have brought a new suit in either the State or Federal Court with proper parties. We cannot understand what fund the filing of the complaint created more than already existed under the policies themselves.

The petitioners place great stress on *Sherman v. Buckley, 119 F. (2d) 280.* The facts of that case differ so materially from our case that a short discussion of it would seem in order.

In *Sherman v. Buckley,* Judge Hand said that the trustee had one of three alternatives available. He could have himself substituted as the plaintiff in the action, or, he could take over the prosecution of it, leaving the bankrupt as the plaintiff, or he could have discontinued and made other disposition of his rights.

Vance, the trustee here, chose the first alternative, not the second, which the trustee chose in the case under discussion by Judge Hand.

It is noteworthy that in the *Sherman v. Buckley* case, Section 475, of the Judiciary Law of New York, was before the Court, which statute has to do with a charging lien of attorneys and of which we have no countedpart in New Mexico.

In the opinion, Judge Hand says "We need not, and we do not, hold, therefore, that if the trustee had brought Buckley and Buckley summarily into the bankruptcy court and insisted upon the liquidation of their lien, preparatory, for example, to a discontinuance or settlement of the action, they would have had any defense."

In our case, Vance, the trustee, did not avail himself of the second alternative. Before the necessary parties were even named in the pleadings and before the insurance companies had answered, he exercised his right to take over the cause of action as an asset of the bankrupt's estate and to substitute himself as the party plaintiff, with new lawyers, thus relieving Jackson and Horan. He took no action which in equity and good conscience should estop the trustee from questioning the amount and value of Jackson and Horan's services, nor has he ever done so, except to insist below and here, that District Judge Neblett's direc-

tion to Jackson and Horan, that they go into the referee's Court and submit their claim of lien to that tribunal, just as Judge Hand says the trustee might have done had he so elected, is correct.

We are unable to see how *Sherman v. Buckley* can be cited as establishing the rule that the trustee in bankruptcy in order to avail himself of his right to be substituted, with new counsel, in a State Court case, for the recovery of assets belonging to the bankrupt's estate, must, as a condition precedent, agree that the State Court shall exercise a supervisory control over the administration by the Bankruptcy Court of the proceeds of an unliquidated claim if, as and when received.

There are many situations in which it is to the advantage of the trustee and the estate of the bankrupt to take over and continue in the name of the trustee pending State Court litigation. If this were not true, the alternative would not be included in the bankruptcy law, but to add to this statutory right of the trustee the burden of consenting to a joint administration of the fund between the State Court and the Bankruptcy Court would produce endless confusion.

As to the cases of *In Re Prudence, 96 F. (2d) 157,* and *In Re San Juan Gold, Inc. 96 F (2d) 60,* we are not able to see how they are applicable here. In the *Prudence* case the attorney had prosecuted his client's claim to judgment and an appeal was pending when the client went into bankruptcy to reorganize under 77-b. The trustees allowed the bankrupt's attorney to go ahead with the second trial, knowing the fee arrangement, and when a recovery was made through the lawyer's efforts, the trustee sought to dispute his right to his fee. Such inequitable conduct is

certainly reprehensible and no element like it is present in our case.

In the *San Juan Gold, Inc.* case, a lawyer had possession of the books and records of his client, and when the Federal Court ordered him to turn them over without taking any testimony as to the value of his services, the Circuit Court of Appeals reversed and correctly held that the attorney had a right to be heard, but that hearing was not to be in the State Court but in the Bankruptcy Court, just as Federal Judge Neblett ordered in our case, both by the ruling of October 25, 1948 (Tr. 3-5), and again in his order of February 15, 1949, (Tr. 10-12).

At no point in the proceedings has the District Court nor the Court of Appeals sought to prevent Jackson and Horan from appearing in the Bankruptcy Court and giving evidence to the extent of their claim of lien, but they have insisted that the matter is not one for examination and adjudication by the Bankruptcy Court, but that they come in before the referee with the State Court order as res adjudicata of the nature and extent of their rights, which, of course, is a trespass upon the jurisdiction of the Federal Court (Tr. 6).

## POINT IV

Under this Point, the petitioners say the District Court erred in holding the State Court order of August 21, 1947, a nullity insofar as it awarded Jackson and Horan the charging and retaining lien.

First, under this Point, the petitioners claim that *Nehr v. Crawford, 10 N. M. 725, 65 P. 156,* is authority for the

statement that the State Court order of August 21, 1947, was appealable, and since no appeal was taken, is final. They quote in the index excerpts from the Rules of Civil Procedure of the District Courts of the State of New Mexico, found in *19-201 (5) of the New Mexico Statutes Annotated, 1941,* official edition. We are surprised that petitioners have not quoted the second section of the same Rule, which reads as follows:

> "2. Appeals shall also be allowed by the District Court and entertained by the Supreme Court in all civil actions from such interlocutory judgments, orders or decisions of the District Court as practically dispose of the merits of the action, so that any further proceeding therein would be only to carry into effect such interlocutory judgment, order or decision. * * * * Application for allowance of an appeal under the provisions of this section must be made within twenty days from the entry of the judgment, order, decision or conviction appealed from."

Was the State Court's order of August 21, 1947, overruling Jackson & Horan's motion to strike the trustee's motion to be substituted, and sustaining the trustee's motion for substitution, and adjudging and fixing a charging and retaining lien of Jackson and Horan in the amount of 15% of the recovery, a final order? It could not have been, because there were no defendants in court and the struggle was between the bankrupt and his lawyers on one side, and the trustee and his lawyers on the other, seeking control of the case.

Was this an interlocutory order such as practically disposed of the merits of the action, so that any proceeding therein would be only to carry into effect the judgment, order or decision? Again we say that the order had no such

effect and did not purport to do so. It was merely disposing of the matter of who should continue the litigation as plaintiff before the defendants had answered, and was not an appealable order.

Judge Bratton, who wrote the opinion of the Court of Appeals, which petitioners seek to review in this proceeding by certiorari, and Judge Phillips who concurred with him, were both New Mexico practitioners, and they had no hesitation in holding that the State Court order substituting the trustee as plaintiff and attempting to fix a lien on the recovery entered on August 21, 1947, was not appealable, either under the ninety day provision for final judgments or under the twenty day rule for interlocutory judgments, which had the effect or practically disposing of the case.

The purpose of the litigation was to bring before the State Court the three insurance companies under an allegation that they had written policies and had refused to pay the loss, and for the purpose of determining the extent of it. That was the whole substance of the litigation and it had not even reached the stage where the pleadings had been settled or the defendants had appeared.

Judge Bratton cites in support of this holding, *Burns v. Fleming, 48 N. M. 40, 145 Pac. (2d) 861; Foster v. Addington, 48, N. M. 212, 148 Pac. (2) 373.*

Since it appeared from the face of the State Court order substituting the trustee, that Stuart had theretofore been adjudged a bankrupt and Vance was his duly elected trustee, it remains to consider whether, or not, so much of that order as attempted to establish and charge the ultimate collection with a lien in favor of Jackson and Horan,

was void upon its face and could not constitute res adjudicata, as Judge Bratton, in his opinion, held. This brings us to the main question presented by the application of the petitioners. This is whether *Gross v. Irving Trust Co., 286 U. S. 342, and Taylor v. Sternberg, 293 U. S. 470,* are still the law, and what their effect will be when applied to the record here. We fail to see how stronger language could have been used than was employed by the Court in the *Gross* case, saying that the filing of a bankruptcy petition is a caveat to all the world and, in fact, an attachment and an injunction; and further holding that the jurisdiction of the Bankruptcy Court is paramount. So District Judge Neblett held in his orders of October 25, 1948 (Tr. 3-5) and February 15, 1949 (Tr. 10-12).

This case does not present any of the features sometimes presented in State Court receiverships referred to in the *Gross* case, where comity requires the trustee to call attention of the State Court to the paramount jurisdiction of the Bankruptcy Court and request the setting aside of conflicting orders. While this presupposes that the State Court will immediately relinquish jurisdiction and abate such orders as may be in conflict, the ultimate power and authority of the Bankruptcy Court, under its exclusive jurisdiction, cannot be questioned.

## POINT V

This Point seems to have been eliminated by the opinion of the Court of Appeals holding that a void order of the State Court, after exclusive jurisdiction had passed to the Bankruptcy Court, was a nullity. It could not have been res adjudicata. And since it was not a final judgment

appealable within the ninety day rule, nor an interlocutory judgment having the effect of practically disposing of the merits of the case, within the twenty day rule, it was not appealable.

If it was void, the subsequent appearance of the Bank as a defendant and cross-complainant in the litigation, could not have the effect of preventing the Bank, or the trustee, from calling attention to the void nature of the order.

## CONCLUSION

Denial of certiorari in the *Sherman* case is, as we understand the rule, nothing more than the decision of this Court to the effect that the record presented no necessity for review.

Petitioners here are, in effect, saying that because Judge Hand, in the *Sherman* case, held the trustee must pay the attorney's fees, under the circumstances there presented by the second alternative course of action available to the trustee, it necessarily follows that in our case the trustee and the Bankruptcy Court must submit to the State Court order in a case where the trustee chose the first alternative as his course.

If the position of the petitioners is correct the statutory right under the bankruptcy act of a trustee to substitute himself and his own attorneys in State Court litigation, and to oust the bankrupt and his counsel therefrom, must be purchased by the trustee at the price of submitting to the orders of the State Court not only as to the conduct of the litigation but also as to the distribution of the proceeds when realized. If this be the law, then *Gross v. Irving*

*Trust Company* must be overruled and the exclusive jurisdiction of the Bankruptcy Court must be repudiated.

We submit that the petition for the writ of certiorari should be denied.

Respectfully submitted,

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